

## **2009 DRAFTING REQUEST**

### **Bill**

Received: **12/18/2008**

Received By: **jkreye**

Wanted: **As time permits**

Identical to LRB:

For: **Administration-Budget**

By/Representing: **Lillethun**

This file may be shown to any legislator: **NO**

Drafter: **jkreye**

May Contact:

Addl. Drafters:

Subject: **Tax, Other - sales**

Extra Copies:

Submit via email: **NO**

---

### **Pre Topic:**

DOA:.....Lillethun, BB0289 -

---

### **Topic:**

Disregarded entities

---

### **Instructions:**

See attached

---

### **Drafting History:**

<u>Vers.</u>	<u>Drafted</u>	<u>Reviewed</u>	<u>Typed</u>	<u>Proofed</u>	<u>Submitted</u>	<u>Jacketed</u>	<u>Required</u>
/?	jkreye 12/18/2008	kfollett 12/19/2008		_____			State
/1	chanaman 02/11/2009	kfollett 02/12/2009	mduchek 12/19/2008	_____	mbarman 12/19/2008		State
/2			jfrantze 02/12/2009	_____	cduerst 02/12/2009		

FE Sent For:

<END>

## 2009 DRAFTING REQUEST

### Bill

Received: 12/18/2008

Received By: jkreye

Wanted: As time permits

Identical to LRB:

For: Administration-Budget

By/Representing: Lillethun

This file may be shown to any legislator: NO

Drafter: jkreye

May Contact:

Addl. Drafters:

Subject: Tax, Other - sales

Extra Copies:

Submit via email: NO

---

### Pre Topic:

DOA:.....Lillethun, BB0289 -

---

### Topic:

Disregarded entities

---

### Instructions:

See attached

---

### Drafting History:

<u>Vers.</u>	<u>Drafted</u>	<u>Reviewed</u>	<u>Typed</u>	<u>Proofed</u>	<u>Submitted</u>	<u>Jacketed</u>	<u>Required</u>
/?	jkreye 12/18/2008	kfollett 12/19/2008					State
/1		12/15/2008 2/12	mduchek 12/19/2008		mbarman 12/19/2008		

FE Sent For:

2/19  
<END>

**2009 DRAFTING REQUEST**

**Bill**

Received: **12/18/2008**

Received By: **jkreye**

Wanted: **As time permits**

Identical to LRB:

For: **Administration-Budget**

By/Representing: **Lillethun**

This file may be shown to any legislator: **NO**

Drafter: **jkreye**

May Contact:

Addl. Drafters:

Subject: **Tax, Other - sales**

Extra Copies:

Submit via email: **NO**

---

**Pre Topic:**

DOA:.....Lillethun, BB0289 -

---

**Topic:**

Disregarded entities

---

**Instructions:**

See attached

---

**Drafting History:**

<u>Vers.</u>	<u>Drafted</u>	<u>Reviewed</u>	<u>Typed</u>	<u>Proofed</u>	<u>Submitted</u>	<u>Jacketed</u>	<u>Required</u>
/?	jkreye	11kjf 12419		_____ _____			

FE Sent For:

**<END>**

1219

## 2007-09 Budget Bill Statutory Language Drafting Request

- Topic: Tax Treatment of Disregarded Entities
- Tracking Code: BB0289
- SBO team: Tax, Transportation and Budget Development Team
- SBO analyst: Chad Lillethun
  - Phone: 266-7597
  - Email: Chad.Lillethun@wisconsin.gov
- Agency acronym: DOR
- Agency number: 566
- Priority (Low, Medium, High): Low

### Intent:

Require law to treat companies that are disregarded for federal or Wisconsin income or franchise tax purposes as disregarded for Wisconsin sales and use tax purposes.

**2009-2011 Legislative Proposal  
Wisconsin Department of Revenue  
IS&E Division**

**Date:** November 7, 2008

**TITLE: Sales and Use Tax Treatment of Disregarded Entities**

**DESCRIPTION OF CURRENT LAW AND PROBLEM**

*de printer*  
A disregarded entity is a business entity with a single owner that chooses to be regarded as unified with its owner (i.e. the entity is "disregarded") for income/franchise tax purposes. The disregarded entity reports its income/franchise tax liability on the return of its owner and the owner is subject to the tax on the disregarded entity's income.

*Conflict*  
In 1997 Act 27, Wisconsin amended and created various tax statutes to adopt federal provisions in order to allow certain single-owner entities to be disregarded as separate entities for Wisconsin income and franchise tax purposes. Two sales and use tax provisions were also amended. One change resulted in disregarded entities being treated as entities separate from their owner for sales and use tax purposes. The other change required the disregarded entity to report its taxable sales and purchases on its owner's return.

This means that while disregarded entities are not considered separate from their owner for Wisconsin income/franchise tax purposes, they are considered separate from their owner for sales/use tax purposes yet file one sales/use tax return (i.e. receipts are reported on the owner's return).

Separate entity sales/use treatment for these disregarded entities has encouraged some businesses to engage in a number of sales and use tax avoidance strategies. Some of these strategies have become common practice. Examples include:

- Trucks Hauling Owners' Product Avoid Tax. Separate transportation company created solely to haul products for the owner. Owner would owe tax on trucks, trailers, etc. purchased to haul its own property, but separate transportation company qualifies for common/contract carrier exemption under sec. 77.54(5)(b), Wis. Stats. if it uses the trucks, etc. exclusively to haul property of others (for example, the owner) for hire.
- Resale for Minimal Amount Avoids Tax. Property may be purchased without tax for resale by separate entity and sold to owner for \$1 (or other nominal amount). Sales tax is owed only on the \$1 sale.
- Materials Used to Manufacture Avoid Tax. Manufacturer creates company to install its products in real property construction in other states to avoid paying tax on purchases of materials used in manufacturing the products (sec. 77.54(2), Wis. Stats.). The manufacturer would owe Wisconsin tax on the materials if it did not create the separate entity to install the products.
- Materials Used in Real Property Construction Avoid Tax. Construction contractors owe tax on materials used in real property construction for exempt entities. By creating a separate supply company; however, the materials go untaxed. The supply company purchases the materials without tax for resale, and the sale of the materials to the exempt entity is exempt under sec. 77.54(9a), Wis. Stats. (2005-06).

- Transfer of Assets Avoids Tax. Aircraft and other expensive assets may be sold without tax under "non-sale" provisions in sec. 77.51(14g), Wis. Stats. (2005-06), by creating shell companies to distribute such assets. The result is that no sales or use tax is due on the sale or purchase of the aircraft (or other asset). For example, Company A purchases an aircraft in a state that does not charge sales tax. Company A sets up a disregarded entity (shell company) and distributes the aircraft to the shell company prior to bringing the aircraft into Wisconsin. Since Company A did not make any use of the aircraft in Wisconsin, Company A is not liable for Wisconsin use tax on its purchase of the aircraft. The distribution of the aircraft from Company A to the shell company meets the "non-sale" provisions; therefore, the distribution of the aircraft to the shell company is not subject to Wisconsin sales tax. The shell company does not owe Wisconsin use tax on the aircraft that it received in the nontaxable transaction.

## **RECOMMENDATION FOR ACTION**

Amend the law to treat companies that are disregarded for federal or Wisconsin income or franchise tax purposes as disregarded for Wisconsin sales and use tax purposes.

## **ADMINISTRATIVE IMPACT**

None.

## **FAIRNESS /TAX EQUITY**

Entities that are disregarded for Wisconsin income and franchise tax purposes would also be disregarded for sales and use tax purposes, providing consistency between these tax types. The disregarded entity would no longer be treated as a separate entity for Wisconsin sales and use tax purposes, thus eliminating the tax avoidance methods currently being used.

## **IMPACT ON ECONOMIC DEVELOPMENT**

None.

## **FISCAL EFFECT**

Assuming use of the strategy has reduced growth in sales and use taxes by 0.5% per year, if the proposal had been in effect in FY08, sales and use taxes would have been \$21.3 million (\$4.269 billion x 0.5%) greater than they were in FY08.

Assuming an effective date of September 1, 2009 and continued 2% growth in annual sales tax collections (consistent with the FY09 growth estimated by the LFB as of 2/13/08), sales and use taxes would increase \$18.5 million in FY10 and \$22.7 million in FY11.

County and stadium sales taxes were approximately 7.7% of state sales tax collections in FY07. Assuming this percentage remains constant, distributions of county and stadium sales and use taxes are estimated to increase approximately \$1.4 million in FY10 and by \$1.7 million in FY11 under the proposal.

## **DRAFTING INSTRUCTIONS**

Amend sec. 77.51(10), Wis. Stats., by removing the last sentence, which currently reads that "[p]erson' also includes the owner of a single-owner entity that is disregarded as a separate entity under ch. 71."

Add the following sentence to Subchapter III of Ch. 77:

"A single-owner entity that is disregarded as a separate entity under ch. 71 is also disregarded as a separate entity for purposes of this subchapter."

See 2009 LRB 539/P1.

#### **EFFECTIVE DATE AND/OR INITIAL APPLICABILITY**

Effective upon publication.

#### **INTERESTED/AFFECTED PARTIES**

Disregarded entities that are using this entity structure as a tax avoidance strategy are expected to oppose this change.

#### **DOR CONTACT PERSON**

Diane Hardt, Division Administrator  
(608) 266-6798

#### **PREPARED BY**

Janet Abrams

Fiscal Estimate prepared by Blair Kruger, R&P Division

12/19/11  
in stays

DOA Budget

BB0289

PRELIMINARY DRAFT - NOT READY FOR INTRODUCTION

in 12-18-08

Don't Gen

1 AN ACT ...; relating to: the budget.

---

*Analysis by the Legislative Reference Bureau*

**TAXATION**

**OTHER TAXATION**

This bill provides that a single-owner entity that is disregarded as a separate entity for income and franchise tax purposes is disregarded as a separate entity for sales and use tax purposes.

For further information see the *state* fiscal estimate, which will be printed as an appendix to this bill.

---

*The people of the state of Wisconsin, represented in senate and assembly, do enact as follows:*

2 SECTION 1. 77.51 (10) of the statutes is amended to read:

3 77.51 (10) "Person" includes any natural person, firm, partnership, limited  
4 liability company, joint venture, joint stock company, association, public or private  
5 corporation, the United States, the state, including any unit or division of the state,  
6 any county, city, village, town, municipal utility, municipal power district or other



1 governmental unit, cooperative, unincorporated cooperative association, estate,  
2 trust, receiver, personal representative, any other fiduciary, and any representative  
3 appointed by order of any court or otherwise acting on behalf of others. "Person" also  
4 includes the owner of a single-owner entity that is disregarded as a separate entity  
5 under ch. 71.

6 **SECTION 2.** 77.61 (16) of the statutes is created to read:

7 77.61 (16) A single-owner entity that is disregarded as a separate entity under  
8 ch. 71 is disregarded as a separate entity for purposes of this subchapter.

9 (END)



State of Wisconsin  
2009 - 2010 LEGISLATURE

LRB-1219/1

JK:kjf:md

DOA:.....Lillethun, BB0289 - Disregarded entities

FOR 2009-11 BUDGET -- NOT READY FOR INTRODUCTION

don't go

1 AN ACT ...; relating to: the budget.

---

*Analysis by the Legislative Reference Bureau*

**TAXATION**

**OTHER TAXATION**

This bill provides that a single-owner entity that is disregarded as a separate entity for income and franchise tax purposes is disregarded as a separate entity for sales and use tax purposes.

For further information see the *state* fiscal estimate, which will be printed as an appendix to this bill.

---

*The people of the state of Wisconsin, represented in senate and assembly, do enact as follows:*

2 SECTION 1. 77.51 (10) of the statutes is amended to read:

3 77.51 (10) "Person" includes any natural person, firm, partnership, limited  
4 liability company, joint venture, joint stock company, association, public or private  
5 corporation, the United States, the state, including any unit or division of the state,

1 any county, city, village, town, municipal utility, municipal power district or other  
2 governmental unit, cooperative, unincorporated cooperative association, estate,  
3 trust, receiver, personal representative, any other fiduciary, and any representative  
4 appointed by order of any court or otherwise acting on behalf of others. "Person" also  
5 includes the owner of a single-owner entity that is disregarded as a separate entity  
6 under ch. 71.

7 **SECTION 2.** 77.61 (16)<sup>16m</sup> of the statutes is created to read:

8 77.61 (16)<sup>16m</sup> A single-owner entity that is disregarded as a separate entity under  
9 ch. 71 is disregarded as a separate entity for purposes of this subchapter.

10 (END)

Date

LRB-1219/2 dr  
JK:kjf

This draft changes s. 77.61 (16) to s. 77.61 (16)<sup>m</sup>  
because the budget bill already contains<sup>s</sup> a  
creation of s. 77.61 (16).

JK

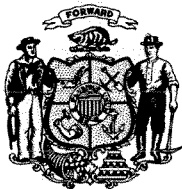
**DRAFTER'S NOTE**  
**FROM THE**  
**LEGISLATIVE REFERENCE BUREAU**

LRB-1219/2dn  
JK:kjfjf

February 12, 2009

This draft changes s. 77.61 (16) to s. 77.61 (16m) because the budget bill already contains a creation of s. 77.61(16).

**Joseph T. Kreye**  
Senior Legislative Attorney  
Phone: (608) 266-2263  
E-mail: [joseph.kreye@legis.wisconsin.gov](mailto:joseph.kreye@legis.wisconsin.gov)



State of Wisconsin  
2009 - 2010 LEGISLATURE

LRB-1219/2

JK:kjf:jf

DOA:.....Lillethun, BB0289 - Disregarded entities

FOR 2009-11 BUDGET -- NOT READY FOR INTRODUCTION

1     **AN ACT ...; relating to:** the budget.

---

*Analysis by the Legislative Reference Bureau*

**TAXATION**

**OTHER TAXATION**

This bill provides that a single-owner entity that is disregarded as a separate entity for income and franchise tax purposes is disregarded as a separate entity for sales and use tax purposes.

For further information see the *state* fiscal estimate, which will be printed as an appendix to this bill.

---

*The people of the state of Wisconsin, represented in senate and assembly, do enact as follows:*

2           **SECTION 1.** 77.51 (10) of the statutes is amended to read:

3           77.51 (10) "Person" includes any natural person, firm, partnership, limited  
4     liability company, joint venture, joint stock company, association, public or private  
5     corporation, the United States, the state, including any unit or division of the state,

1 any county, city, village, town, municipal utility, municipal power district or other  
2 governmental unit, cooperative, unincorporated cooperative association, estate,  
3 trust, receiver, personal representative, any other fiduciary, and any representative  
4 appointed by order of any court or otherwise acting on behalf of others. "Person" also  
5 ~~includes the owner of a single-owner entity that is disregarded as a separate entity~~  
6 ~~under ch. 71.~~

7 **SECTION 2.** 77.61 (16m) of the statutes is created to read:

8 **77.61 (16m)** A single-owner entity that is disregarded as a separate entity  
9 under ch. 71 is disregarded as a separate entity for purposes of this subchapter.

10 (END)